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exogenous cost change in higher prices. For the adoption of FAS 106, we have shown that, in theory, the historical liability for post-retirement benefits would logically already have been captured in the output prices of firms in unregulated markets. To a first approximation, since most of American GNP is produced by firms whose prices reflect economic costs, the accounting change required by FAS 106 will result in no contemporaneous change in the GNP-PI.

Historical experience also suggests that accounting changes have negligible effects on prices in unregulated markets and in the U.S. economy as a whole.²⁴ In 1987, the FASB changed the method of accrual accounting for pension benefits, a change which is similar in principle to the change contemplated in FAS 106, though smaller in magnitude. A search of the empirical literature reveals two studies of the effects of these accounting changes which both show no relationship between accounting changes and stock prices.²⁵ Assuming that (i) changes in stock prices reflect changes in anticipated profits and (ii) changes in accounting costs do not change economic

²⁴Modern finance theory as well as practicing financial analysts recognize that accounting changes do not change the underlying economic reality. For example, in discussing the ramifications of FAS 106, Solomon Samson of Standard & Poor observed, "The realities do not change simply because someone puts down a different number. Part of our trade is adjusting published numbers to reflect economic realities." (BNA Pensions and Benefits Daily, September 27, 1991.)

²⁵NERA undertook a DIALOG Database system search of the relevant literature, including the Economic Literature Index (1969-present), the Academic Index (1976-present), the Conference Papers Index (1973-present), Management Contents (1974-present), and Dissertation Abstracts (1961-present). These databases were searched using as keywords: "FASB," "Financial Accounting Standards Board," "Statement 87," "87," "pensions," and "economic". Fifteen publications were identified and two were relevant: (i) Sheree S. Ma, "An Empirical Examination of the Stock Market's Reaction to the Pension Accounting Deliberations of the Financial Accounting Standards Board," Doctoral Dissertation, University of Alabama, 1989, and (ii) Samuel S. Tung, "Stock Market Reactions to Mandatory Changes in Accounting for Pensions," Doctoral Dissertation, University of Wisconsin, 1987. Both works showed that no changes in stock prices could be attributed to the 1987 pension accounting changes.

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costs, the fact that accounting changes do not affect stock prices implies that accounting changes do not affect output prices.³⁰

To refine this approximation somewhat, we observe that prices of some goods and services will change when FAS 106 is implemented in 1993: notably (i) regulated public utility services and (ii) certain government purchases of services under contracts which historically covered only pay-as-you-go costs and prospectively allow FAS 106 accruals. In 1987, regulated public utilities produced approximately 6.13 percent of U.S. GNP. Total government contract purchases (not just cost-plus contract purchases) were 4.36 percent of GNP in 1987.³¹ In total, what might be called the "cost-plus" sector of the economy produced less than 10.49 percent of GNP in 1987. We use 1987 for comparison because the 1987 government contract data is the latest available. Note that these proportions do not change much over time; Table 1 shows these proportions for 1980 and 1987.³² If all firms experienced the same expense change from FAS 106 in 1993 as Pacific Bell and if prices in the unregulated economy already reflect OPEB costs measured on an economic basis, then the overall price level in the U.S. would increase by less than 0.20 percent in 1993 when accrual accounting is

³⁰This follows from the observations that (i) profits represent the difference between output prices and costs and (ii) accounting changes affect neither profits nor costs.

³¹A GSA report tracks the annual value of Federal Government contracts issued in each year: see General Services Administration, Federal Procurement Data System Standard Report. For 1987, the amount of Federal contracts issued was \$197.3 billion which represents an update (obtained by telephone from the Federal Procurement Data Center) of the published figure.

³²Regulated public utilities include railroad transportation, local and interurban passenger transportation, pipelines other than gas, telecommunications, and electric, gas, and sanitary services. See U.S. Bureau of the Census, Statistical Abstract of the United States: 1990, (110th edition), Washington, D.C., 1990, pp. 425-426. We include data for 1980 to show that the industry components of GNP are reasonably stable over time.

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Table 1.
Relative Size of the Cost-Plus Sector

	GNP by Industry current \$ billion 1980		GNP by Industry current \$ billion 1987	
GNP	\$2,732.0	(percent)	\$4,526.7	(percent)
Railroad	\$20.8		\$19.6	
Passenger transit	\$5.4		\$8.1	
Non-gas pipelines	\$4.7		\$5.3	
Telecommunications	\$60.2		\$108.3	
Electric, gas, sewer	\$68.4		\$136.4	
TOTAL UTILITIES	\$159.5	5.84%	\$277.7	6.13%
GOVERNMENT CONTRACTS			\$197.3	4.36%
TOTAL COST-PLUS SECTOR			\$475.0	10.49%

implemented.³³ Under these assumptions, less than 10.49 percent of Pacific Bell's exogenous cost change would be accounted for in the GNP-PI, and the required Z factor would exceed 89.51 percent of the exogenous cost change.³⁴ This estimate is unrealistic because all U.S. firms have not used OPEBs to the extent that Pacific Bell has.

An additional refinement to this upper bound would recognize that the effect of FAS 106 on Pacific Bell is far greater than on the typical firm in the U.S.

³³Pacific Bell expenses will increase 1.92 percent. If all cost-plus firms have the same proportional OPEB liability as Pacific Bell, the average liability will be a weighted average of 1.92 percent in the cost-plus sector and 0 elsewhere. Thus $(1.92 * 0.1049) + (0.0 * 0.8951) = 0.20$. Recall that this estimate is an upper bound because (i) all government contract purchases are included in the cost-plus sector, not just government purchases under cost-plus contracts, and (ii) the impact of FAS 106 on Pacific Bell is greater than on an average firm.

³⁴10.49 percent equals $0.20/1.92$; and 89.51 percent equals $1.72/1.92$.

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economy. In order to understand what the important differences are, we engaged William M. Mercer, a leading employee benefits consulting firm, to develop and analyze basic facts about post-retirement benefits other than pensions. The most important differences between Pacific Bell and a typical firm appear to be the following:

1. Coverage: Pacific Bell provides post-retirement benefits to its entire pension-qualified labor force. In contrast, only about 40 percent of private sector workers are employed by firms that offer post-retirement health benefits.³⁵
2. Historical liability: Pacific Bell estimates that its accumulated historical postretirement benefit obligation will be about \$0.5 billion in 1993 in the interstate jurisdiction. This amount is about 33 percent of Pacific's annual interstate revenues, about 21 percent of Pacific's interstate net rate base, and about 37 percent of the equity component of the net rate base. In contrast, the accumulated historical liability for the U.S. economy is estimated at about \$300 billion.³⁶ This amount represents about five percent of U.S. GNP and on the order of 7 to 10 percent of corporate equity.³⁷

U.S. OPEB expenses are estimated to be about \$13 billion in 1993 on a cash accounting basis compared with about \$82 billion on an accrual basis in 1993.³⁸ The

³⁵United States General Accounting Office, "Extent of Companies' Retiree Health Coverage," Prepared for Congress, March 1990 (GAO-1990).

³⁶Statement of Gregory J. McDonald, United States General Accounting Office, Before the Subcommittee of Health, Ways and Means Committee of the House of Representatives, May 6, 1991.

³⁷U.S. General Accounting Office, "Companies' Retiree Health Liabilities Large, Advance Funding Costly," Report to Congress, June 1989 (GAO-1989). Mark Warshawsky, "The Uncertain Promise of Retiree Health Benefits: An Evaluation of Corporate Obligations," Retiree Health Benefits Seminar, American Enterprise Institute, Washington, D.C., April 9, 1991.

³⁸Mercer first evaluated a number of existing studies of corporate obligations for OPEBs and concluded that the GAO-1991 study was the most reliable in terms of credibility and methodology. This study produced an estimate of \$42 billion for accrual accounting expenses under FAS 106 procedures in 1991. Mercer then modified a number of assumptions to conform more closely with FAS 106 requirements and carried the calculations forward to 1993, in the process producing the higher figure.

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change is thus \$69 billion out of an estimated GNP of \$6,260 billion, or 1.10 percent.³⁹ Since the incidence of OPEBs appear to be uniformly distributed across industries, it is reasonable to assume that firms in the cost-plus sector increase prices by 1.10 percent in response to FAS 106.⁴⁰ Firms in the rest of the economy have already reflected accrual accounting in their prices, so the net effect of FAS 106 on the GNP-PI would be less than 0.12 percent (twelve-hundredths of one percent) instead of the 0.20 percent bound calculated above.⁴¹ Thus, if cost-plus firms experience the U.S. average OPEB expense increase (1.10 percent) instead of the Pacific Bell increase (1.92 percent), GNP-PI would increase by less than 0.12 percent and the required Z factor would exceed 1.80 percent. Thus, less than 6.26 percent of the exogenous cost change is reflected in the GNP-PI, leaving more than 93.74 percent to be recovered through the Z factor.⁴²

This estimate of the effect of FAS 106 on the GNP-PI is an upper bound for several reasons. First, we have overstated the size of the cost-plus sector of the economy by assuming that all public utility prices are set using accounting costs and treating all government contracts as cost-plus contracts with accounting change escalators. Second, this calculation ignores second-order effects that would lower the impact on national output prices. As prices rise in the cost-plus sector, for example,

³⁹The 1993 GNP forecast was downloaded from Data Resources, Inc.

⁴⁰A GAO survey in 1990 compared health coverage of retirees by type of industry and concluded that there was "little variation among companies with retiree health benefits when comparing companies by industry group," GAO-1990 Report, pp. 6-7. Thus the impact of FAS 106 on expenses for firms in the cost-plus sector should be roughly the same as the U.S. average of 1.10 percent.

⁴¹Thus $(1.10 \cdot 0.1049) + (0.0 \cdot 0.8951) = 0.12$ percent.

⁴²Because $[1.92 - 0.12]/1.92 = 93.74$ percent and $0.12/1.92 = 6.26$ percent.

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consumers substitute away from these goods and services which reduces the net effect of the price increase in the cost-plus sector on overall inflation. Finally, the calculation ignores second-order macroeconomic responses to the change in output prices through changes in government expenditure, interest rates and the money supply.

A summary of these calculations may be useful. Recall that we wish to increase Pacific Bell's price cap by 1.92 percent which represents the change in expenses due to the shift from cash to accrual accounting for OPEBs in 1993. Some of this increase will be accounted for by the change in inflation; the rest must be supplied through the Z-adjustment we are calculating. The increase in inflation due to FAS 106 is measured in two steps: (i) we calculate the effect of FAS 106 on the expenses of an average firm to be 1.10 percent, and (ii) we calculate the fraction of GNP produced by firms whose prices do not already reflect accrual accounting for OPEBs to be less than 10.49 percent. Since the incidence of OPEBs across industries is roughly constant, we estimate that the prices at which less than 10.49 percent of GNP is sold will increase by 1.10 percent, so that the increase in GNP-PI, averaged over all firms, will be less than 0.12 percent. Using this bound as an estimate, Pacific Bell's 1.92 percent price increase would thus consist of a 0.12 percent increase in GNP-PI and a 1.80 percent Z-adjustment. The required Z-adjustment (net of the change in GNP-PI) is thus at least 93.74 percent of the \$29 million change in expenses, or at least \$27 million.

These results are stable with respect to the various assumptions and forecasts that we have made. In Table 2, we summarize our previous results and provide new estimates assuming (i) a 100 percent increase in the effect of FAS 106 on an average

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Table 2
Summary of Results
and
Sensitivity Analysis

	BASE CASE	NATIONAL FAS EFFECT IS 100% LARGER	COST-PLUS SECTOR IS 100% LARGER	PB REVENUE FORECAST IS 10% LARGER
PAC BELL FAS EFFECT	1.92%	1.92%	1.92%	1.74%
GNP-PI EFFECT	0.12%	0.23%	0.23%	0.12%
Z-ADJUSTMENT	1.80%	1.69%	1.69%	1.62%
% FAS IN GNP-PI	6.26%	12.01%	12.01%	6.89%
% FAS IN Z	93.74%	87.99%	87.99%	93.11%
Z	\$26,808	\$25,166	\$25,166	\$26,629

U.S. firm, (ii) a 100 percent increase in the cost-plus proportion of the U.S. economy, and (iii) a 10 percent increase in our forecast of Pacific Bell's 1993 revenues. Clearly, the results are insensitive to the assumptions.

APPENDIX

In this Appendix, we provide the details of the derivation of the price cap annual adjustment formula. The logic follows that of Dr. Schankerman, whose presentation of the price cap formula formed the basis of the California price cap plan.⁴³

A. The Relationship Among TFP, Input Price, and Output Price Growth

Consider a multiproduct firm having N outputs (Q_i^o , $i=1,...,N$) and M inputs (Q_j^i , $j=1,...,M$). We wish to calculate X and Z so that in all periods, economic profits are identically zero, i.e., that the value of total inputs (including a normal return on capital) equals the value of total output. The identity can be written as

$$\sum_{i=1}^N p_i Q_i^o = \sum_{j=1}^M w_j Q_j^i,$$

where p_i and w_j denote output and input prices respectively. Differentiating this identity with respect to time yields

$$\sum_{i=1}^N p_i Q_i^o + \sum_{i=1}^N p_i \dot{Q}_i^o = \sum_{j=1}^M w_j Q_j^i + \sum_{j=1}^M w_j \dot{Q}_j^i,$$

⁴³Testimony of Mark Schankerman on behalf of GTE California Incorporated, Docket I. 87-11-033, Technical Appendix, pp. 1-3.

Appendix Page 2

where a dot indicates a derivative with respect to time. Dividing both sides of the equation by the value of output $R = \sum_i p_i Q_i^o$ or $C = \sum_j w_j Q_j^i$, we obtain

$$\sum_i p_i \left(\frac{Q_i^o}{R} \right) + \sum_i Q_i^o \left(\frac{p_i}{R} \right) = \sum_j w_j \left(\frac{Q_j^i}{C} \right) + \sum_j Q_j^i \left(\frac{w_j}{C} \right),$$

where R and C denote revenue and cost. If r_i denotes the revenue share of output i and c_j denotes the cost share of input j , then

$$\sum_i r_i dp_i = \sum_j c_j dw_j - \left[\sum_i r_i dQ_i^o - \sum_j c_j dQ_j^i \right],$$

where d denotes a percentage growth rate: $dp_i = \dot{p}_i / p_i$. The first term in the above equation is the revenue weighted average of the rates of growth of output prices, and the second is the cost-weighted average of the rates of growth of input prices. The term in brackets is the difference between the rates of growth of weighted averages of outputs and inputs and is thus the change in TFP. We can write the equation as

$$dp = dw - dTFP.$$

Thus the growth in input prices less the growth in output prices is equal to the change in TFP. This result requires only that excess profits are zero in every period. It does not require cost minimization, profit maximization, marginal cost pricing, or constant returns to scale.

B. The Price Cap Adjustment Equation

We begin with equation (3) from the text:

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$$(6) \quad dp = dp^N - [dTFP - dTFP^N + dw - dw^N] + [Z^* - Z^{*N}].$$

If we measure national output price inflation by the change in GNP-PI, we obtain

$$(7) \quad dp = GNP-PI - X + Z'$$

where $X = [dTFP - dTFP^N] + [dw - dw^N]$ and $Z' = Z^* - Z^{*N}$. Since the percentage change in the regulated firm's output price between years t-1 and t is just $[p_t - p_{t-1}] / p_{t-1}$, we can write equation (7) as

$$\frac{p_t - p_{t-1}}{p_{t-1}} = GNP-PI - X + Z'$$

so

$$p_t - p_{t-1} = p_{t-1} \times [GNP-PI - X + Z']$$

which simplifies to

$$(8) \quad p_t = p_{t-1} \times [1 + GNP-PI - X + Z'].$$

Since revenue equals price times quantity, the revenue change associated with the price change in equation (8) is obtained by multiplying both sides of the equation by the fixed amount of quantity demanded:

$$q_{t-1} \times p_t = q_{t-1} \times p_{t-1} \times [1 + GNP-PI - X + Z']$$

or

$$(9) \quad R_t = R_{t-1} \times [1 + GNP-PI - X] + Z$$

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where Z represents the total dollar value of the exogenous cost change rather than the unit cost change.

Appendix E

Issue A: Response to Paragraph 17

1. The date the company implemented SFAS-106.

January 1, 1993

2. The cost basis of the pay-as-you-go amounts that supported the rates in effect on the initial date that the carrier became subject to price cap regulation.

\$451,000

3. The effect of the price cap formula on that amount up to the conversion to SFAS-106.

1991 GNP-PI = 4.80%
1991 X = 3.30%
1992 GNP-PI = 3.40%
1992 X = 3.30%

Effect = $\$451,000 * (1 + 0.048 - 0.033) * (1 + 0.034 - 0.033) -$
 $\$451,000$
= $\$451,000 * 1.015 * 1.011 - \$451,000$
= \$7000

4. The carrier's actual cash expenditures related to SFAS-106 for each year since the implementation of price caps, but prior to implementation of SFAS-106 accounting methods.

None

5. The treatment of these costs in reports to the Securities and Exchange Commission (SEC) and to shareholders, including specific citations to or exempted materials from, such reports to indicate the amount of liability each party has projected in OPEBs.

Attached to this Appendix are relevant excerpts from the 1992-93 Forms 10K and Annual Reports for Rochester Telephone Corporation and the 1994 Form 10K and Annual Report for Frontier Corporation.

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934 [Fee Required]

For the fiscal year ended December 31, 1992

Commission file number 1-4166

ROCHESTER TELEPHONE CORPORATION

(Exact Name of registrant as specified in its charter)

New York
(State or other jurisdiction of
incorporation or organization)

16-0613330
(I.R.S. Employer Identification No.)

180 South Clinton Avenue
Rochester, New York
(Address of principal executive offices)

14646-0700
(Zip Code)

(716) 777-7100
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of Class</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$1.00 per share	New York Stock Exchange
4 1/4 Percent Convertible Debentures Due March 1, 1994	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

The aggregate market value of the voting stock held by non-affiliates of the registrant as of February 28, 1993 is \$1,244,351,897.

The number of shares outstanding of Rochester Telephone Corporation's common stock (Par Value \$1.00 per share) as of the close of February 28, 1993 is 33,325,800 shares.

Telephone Company resulted in the following: the elimination of the state tax adjustment surcharge on a go-forward basis, flow through of state deferred taxes on a prospective basis and amortization of the embedded balance over three years, amortization of the reserve deficiency from the purchase of a switch over three years, and a mutual stay-out for three years, i.e. Canton may not file for a rate increase nor can the PAFUC issue another Order of Show Cause against Canton for three years. The Joint Petition was approved by the PAFUC effective December 17, 1992.

On November 4, 1992, Fairmount Telephone Company filed two requests with the Georgia Public Service Commission (GPSC). The first request is for an increase in Hardship Assistance Fund payments from \$.2 million to \$.3 million per year, effective January 1, 1993, at which time the current payments are due to expire. The second request is for a rate increase of \$.5 million per year, which would be reduced by the amount of Hardship Assistance Fund payments granted by the GPSC, and would be withdrawn for six months if the full Hardship Assistance request is granted. The company has since filed a letter with the GPSC to combine the company's Hardship Assistance Filing with its Rate Case filing, resulting in the Rate Case filing being the surviving document.

The Mississippi Public Service Commission (MSPSC) issued an Order to Show Cause, requiring Mid-South Telephone Company to perform an in-house depreciation study. As a result, on January 7, 1993, the MSPSC approved the company's proposed two-year amortization (1992 and 1993) on the \$.5 million unrecovered cost of its analog switch in order to mitigate the Order to Show Cause.

In 1993 the Company will adopt Financial Accounting Standards Board Statement No. 106 (FAS 106), "Employers' Accounting for Postretirement Benefits Other Than Pensions." A significant majority of employees who retire are provided benefits by the Company. It is estimated that the accumulated postretirement benefit obligation (APBO) as of January 1, 1993 is \$126.9 million. If the Company elects to adopt FAS 106 using the delayed recognition of the transition obligation method, the company estimates that its annual expense will be approximately \$18.3 million, versus \$4.1 million using the pay-as-you-go method. If the company adopts the immediate recognition method, the annual expense will be approximately \$12.3 million. The accounting method adopted will be influenced by the rate-making treatment as prescribed for the company's regulated telephone operations by federal and state regulatory agencies.

On January 22, 1993, the Federal Communications Commission (FCC) rejected a petition for recovery of FAS 106 costs through the rate-making process, which impacts approximately 20 percent of the incremental expense for 1993. The decision is being appealed by the Company and others in the industry. A proceeding is underway at the NYSPSC which represents approximately \$9.0 million of the \$18.3 million annual expense using the delayed recognition of the transition obligation method. The outcome of this proceeding cannot be predicted at this time. In addition, the Company believes that the new rules will not negatively impact its net cash flow (or its funding strategy) relating to retiree benefits.

The Company and the NYSPSC entered into a financing agreement, or Stipulation, in 1986 to allow the Company flexibility to pursue acquisitions and to fulfill financing requirements of existing subsidiaries. The Stipulation was amended in 1988 and again in 1991 in conjunction with the acquisition of the Centel telephone properties. Portions of the 1991 amendment

FORM 10-K

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934 [FEE REQUIRED]

For the fiscal year ended December 31, 1993

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934 [NO FEE REQUIRED]

For the transition period from _____ to _____

Commission file number 1-4166

ROCHESTER TELEPHONE CORPORATION

(Exact Name of Registrant as specified in its charter)

NEW YORK

(State or other jurisdiction of
incorporation or organization)

16-0613330

(I.R.S. Employer
Identification No.)

180 South Clinton Avenue
Rochester, New York

(Address of principal executive offices)

14646-0700

(Zip Code)

Registrant's telephone number, including area code: (716) 777-7100

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of each exchange on which registered</u>
Common Stock, par value \$1.00 per share	New York Stock Exchange
4 3/4 Percent Convertible Debentures Due March 1, 1994	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

The aggregate market value of the voting stock held by non-affiliates of the registrant as of February 28, 1994 is \$1,587,600,000. The number of shares outstanding of Rochester Telephone Corporation's common stock (Par Value \$1.00 per share) as of the close of February 28, 1994 is 36,579,066 shares.

DOCUMENTS INCORPORATED BY REFERENCE

- (1) Portions of the registrant's Annual Report to Shareowners for fiscal year ended December 31, 1993, as presented in Exhibit No. 13 of this Form 10-K, are incorporated by reference in Part II hereof.
- (2) Portions of the Notice of Annual Meeting and Proxy Statement issued by the registrant in connection with its Annual Meeting of Shareowners to be held April 27, 1994, as presented in Exhibit No. 99 of this Form 10-K, are incorporated by reference in Parts III and IV hereof.

interstate access charges between the Rochester, New York operating company and the combined subsidiary local telephone companies. This action allowed the company to establish two sets of rates: one based on the specific costs incurred by the Rochester, New York operating company; and one based on the combined cost of the subsidiary local telephone companies, which primarily serve geographic areas currently less subject to competition than the Rochester, New York operating company. On a consolidated basis, the change is initially revenue neutral.

Effective January 1, 1993, the company adopted FAS 106, "Employers' Accounting for Postretirement Benefits Other than Pensions," and petitioned the FCC to recover the FAS 106 costs through the rate-making process. Although the FCC originally rejected the company's petition, the FCC later allowed the company to recover the portion of the FAS 106 cost associated with the Transition Benefit Obligation (the unrecorded postretirement benefit liability) amortized over a twenty year period, pending the FCC's investigation as to whether this cost should be recoverable by price cap regulated companies. Rates reflecting this expense went into effect on July 2, 1993. The FCC's investigation remains pending.

On March 12, 1993, the company signed a definitive agreement to form a joint venture with New York Cellular Geographic Service Area, Inc., a subsidiary of NYNEX Corporation, to create an upstate New York cellular supersystem that will include the Buffalo, Rochester, Syracuse, Utica-Rome and NY Rural Service Area #1 markets. The parties have sought a waiver of the interLATA prohibition contained in the AT&T consent decree, *United States V. American Telephone and Telegraph Co.*, 552 F. Supp. 131 (D.D.C. 1982), *aff'd mem.*, 460 U.S. 1001 (1983). Approval on the waiver request is anticipated in early 1994.

On May 18, 1993, the company filed for approval to form the joint venture from the New York State Public Service Commission. This filing included a petition to transfer the Rochester, New York operating company's interest in the Rochester wireless cellular business to its wholly-owned subsidiary, Rochester Tel Mobile Communications Inc. The Commission approved the entire transaction and transfer at its open session on November 10, 1993 and issued an order dated December 10, 1993.

In addition, the joint venture parties filed applications with the Federal Communications Commission to transfer various radio licenses associated with the cellular properties and anticipate that the approvals will be granted in early 1994. Pending the remaining approvals, Rochester Tel Mobile Communications, Inc. (RTMC) and NYNEX have signed an agreement allowing RTMC to manage the combined properties.

Vista Telephone Company of Minnesota filed a request to increase rates in March 1993 with the Minnesota Public Service Commission. A stipulated settlement was executed by all parties and was submitted for approval to the Minnesota Public Service Commission. The Administrative Law Judge recommended an annual regulated revenue increase of \$4.5 million. The company expects Commission approval during the first quarter of 1994.

The Vista Telephone Company of Iowa filed in August

1993 for a permanent rate increase of approximately \$4.5 million and a temporary rate increase of \$4.1 million. On November 5, 1993, the Iowa State Utilities Board approved the temporary rate increase as submitted. This resulted in an approximate 21 percent across-the-board increase in local service rates. A final order is expected in the second quarter of 1994.

Incentive Regulation

The incentive regulation agreement which the New York State Public Service Commission approved in January 1990 for the Rochester, New York operating company expired at the end of 1992. The Rochester, New York Operating company proposed a new incentive regulation agreement in January 1993 to the Commission staff, and reached a settlement, which was approved by the Commission on January 12, 1994. The settlement reduces the Rochester, New York operating company's revenue requirement by \$5 million in 1993 and \$9.5 million in 1994. Each of these reductions is subject to adjustment for depreciation changes. In 1994, fifty percent of the Rochester, New York operating company's earnings above the authorized return on equity will be shared with ratepayers. The authorized return is currently 10.9 percent and is subject to adjustment based on the results of the Generic Financing Proceeding. Also, if the Rochester, New York operating company's service levels in 1994 drop below 1992 levels, the company will be subject to a penalty of one-half of one percent of its local service revenues.

Acquisitions and Divestitures

On April 15, 1993, the company acquired a 70 percent ownership of the Utica-Rome Cellular Partnership using 702,737 shares of original issue common stock. The transaction was accounted for as a purchase acquisition. In December 1993, the company increased its cellular ownership from 50.6 percent to 69.6 percent in the South Alabama cellular partnership. This later transaction gave the company the right to manage two cellular properties, Alabama RSA #4 and #6, which serve a territory with a population of approximately 252,000.

On June 7, 1993, the Telecommunication Services Group acquired Budget Call Long Distance, Inc. for \$7.5 million in cash. On September 30, 1993, Mid Atlantic Telecom, Inc. was acquired using 143,587 shares of treasury stock. Both transactions were accounted for as purchase acquisitions.

Statesboro Telephone Company of Statesboro, Georgia, with more than 15,000 access lines, was acquired on August 31, 1992. The transaction was accounted for as a pooling of interests. During 1991, four telephone companies representing more than 160,000 access lines were acquired. (See Note 2 to the Consolidated Financial Statements.)

In September 1993, the company sold its interest in the S&A Telephone Company (824 access lines) and its related minority cellular interest in a Topeka, Kansas cellular partnership. In December 1993, the company announced that it had reached a definitive agreement to sell the Minc Telephone Company in North Dakota. Minc serve approximately 25,000 access lines and is the company's only operation in North Dakota. The sale is subject to regulator

10. Service Pensions and Benefits

The company, through various contributory and non-contributory defined benefit pension plans, provides retirement benefits for substantially all employees. Benefits, in general, are based on years-of-service and average salary.

The funded status of the plans is as follows:

<i>In thousands of dollars</i>				
<u>December 31,</u>	<u>1993</u>	<u>1992</u>	<u>1991</u>	
Actuarial present value of benefit obligations:				
Vested benefit obligation	\$283,567	\$243,307	\$227,317	
Accumulated benefit obligation	\$307,016	\$257,893	\$242,464	
Plan assets at fair value, primarily fixed income securities and common stock	\$397,841	\$370,711	\$351,498	
Projected benefit obligation	354,065	316,335	304,730	
Funded status	43,776	54,376	46,768	
Unrecognized net (gain) loss	(28,729)	(42,572)	(40,247)	
Unrecognized net transition asset	(5,442)	(4,941)	(6,512)	
Unrecognized prior service cost	9,227	7,071	12,554	
Pension asset included in Consolidated Balance Sheet	\$ 18,832	\$ 13,934	\$ 12,563	

The net periodic pension cost consists of the following:

<i>In thousands of dollars</i>				
<u>Year Ended December 31,</u>	<u>1993</u>	<u>1992</u>	<u>1991</u>	
Service cost—benefits earned during the period	\$ 7,758	\$ 7,033	\$ 5,464	
Interest cost on projected benefit obligation	23,932	23,123	21,702	
Actual return on plan assets	(40,484)	(24,860)	(63,059)	
Net amortization and deferral	7,623	(9,033)	37,006	
Net periodic pension cost determined under FAS 87	(1,171)	(3,737)	1,113	
Amount expensed due to regulatory agency actions	(1,537)	6,787	2,223	
Net periodic pension cost recognized	\$ (2,708)	\$ 3,050	\$ 3,336	

The projected benefit obligation at December 31, 1993 was determined using an assumed weighted average discount rate of 7.25 percent and an assumed weighted average rate of increase in future compensation levels of 5.0 percent. The weighted average expected long-term rate of return on plan assets was assumed to be 8.75 percent. The unrecognized net transition asset as of January 1, 1987 is being amortized over the estimated remaining service lives of employees, ranging from 12 to 26 years.

The company's funding policy is to make contributions for pension benefits based on actuarial computations which reflect the long-term nature of the pension plan. However, under Financial Accounting Standards Board Statement No. 87 (FAS

87), "Employers' Accounting for Pensions," the development of the projected benefit obligation essentially is computed for financial reporting purposes and may differ from the actuarial determination for funding due to varying assumptions and methods of computation.

During 1993, 1992 and 1991, the company funded \$.2 million, \$4.8 million and \$4.0 million, respectively, for employees' service pensions and certain death benefits.

The company also sponsors a number of defined contribution plans. The most significant plan covers substantially all management employees, who make contributions via payroll deduction. The company matches 75 percent of that contribution up to 6 percent of gross compensation. The total cost recognized for all defined contribution plans during 1993 was \$4.1 million.

On November 30, 1992, a voluntary pension incentive plan was offered to Rochester, New York operating company employees who were pension-eligible and retired on or before December 31, 1992. A 7.5 percent additional pension benefit will supplement the normal pension benefit for up to five years or until age 65, whichever is earlier. Accordingly, pension costs for the fourth quarter of 1992 include a one-time charge of \$.8 million. Payments will be made from pension plan assets.

11. Postretirement Benefits Other Than Pensions

The company provides health care, life insurance, and certain other retirement benefits for substantially all employees. Effective January 1, 1993, the company adopted Financial Accounting Standards Board Statement No. 106 (FAS 106) "Employers' Accounting for Postretirement Benefits Other Than Pensions." FAS 106 requires that employers reflect in current expenses an accrual for the cost of providing postretirement benefits to current and future retirees. Prior to 1993, the company recognized these costs as they were paid. The cost of postretirement benefits was recognized as determined under the projected unit credit actuarial method. Plan assets consist principally of life insurance policies.

In adopting FAS 106, the company elected to defer the recognition of the accrued obligation of \$125 million over a period of twenty years. For 1993, the adoption of this standard resulted in additional operating expenses in the amount of \$7.8 million, net of a deferred income tax benefit of \$4.1 million. However, a substantial portion of this increase was offset by a change in accounting for pensions for rate making purposes at the Rochester company. The change requires that the company amortize, over a ten year period, the cumulative amount of pension funding from January 1, 1987 over the amount of pension expense which would have been recognized through December 31, 1992 under FAS 87, reducing pension expense throughout the amortization period. The net impact of adopting FAS 106 and recording the accounting change for FAS 87 actually resulted in only \$3.8 million of additional operating expenses, net of the income tax benefit, in 1993.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 1994

Commission file number 1-4166

FRONTIER CORPORATION

(Previously Rochester Telephone Corporation)
(Exact name of registrant as specified in its charter)

New York
(State or other jurisdiction of
incorporation or organization)

16-0613330
(I.R.S. Employer
Identification No.)

180 South Clinton Avenue, Rochester, New York
(Address of principal executive offices)

14646-0700
(Zip code)

(716) 777-7100
(Registrant's telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

Title of class	Name of each exchange on which registered
Common Stock, par value \$1.00 per share	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes [☒] No []

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K [☒]

The aggregate market value of the stock held by non-affiliates of the registrant as of March 7, 1995 is \$1,577,641,731.00. The number of shares outstanding of Frontier Corporation's common stock (Par Value \$1.00 per share) as of the close of March 7, 1995 is 72,723,675 shares.

DOCUMENTS INCORPORATED BY REFERENCE

- (1) Portions of the registrant's 1994 Financial Review including MD&A, Consolidated Financial Statements and Notes to Financial Statements, as presented in Exhibit No. 13 of this Form 10-K, are incorporated by reference in Parts II and IV hereof.
 - (2) Portions of the Notice of Annual Meeting and Proxy Statement issued by the registrant in connection with its Annual Meeting of Shareowners to be held April 26, 1995, as presented in Exhibit No. 99 of this Form 10-K, are incorporated by reference in Parts II, III and IV hereof.
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11. Postretirement Benefits Other Than Pensions

The Company provides health care, life insurance, and certain other retirement benefits for substantially all employees. Effective January 1, 1993, the Company adopted Financial Accounting Standards Board Statement No. 106 (FAS 106), "Employers' Accounting for Postretirement Benefits Other Than Pensions." FAS 106 requires that employers reflect in current expenses an accrual for the cost of providing postretirement benefits to current and future retirees. Prior to 1993, the Company recognized these costs as they were paid. Plan assets consist principally of life insurance policies and money market instruments.

In adopting FAS 106, the Company elected to defer the recognition of the accrued obligation of \$125 million over a period of twenty years. For 1993, the adoption of this standard resulted in additional operating expenses in the amount of \$7.8 million, net of a deferred income tax benefit of \$4.1 million.

However, a substantial portion of this increase was offset by a change in accounting for pensions for rate making purposes at the Rochester, New York operating company. The change requires that the company amortize, over a ten year period, the cumulative amount of pension funding from January 1, 1987 over the amount of pension expense which would have been recognized through December 31, 1992 under FAS 87, reducing pension expense throughout the amortization period. The net impact of adopting FAS 106 and recording the accounting change for FAS 87 actually resulted in \$3.8 million of additional operating expenses, net of the income tax benefit, in 1993.

The funded status of the plans is as follows:

<i>In thousands of dollars</i>	December 31,	1994	1993
Accumulated postretirement benefit obligation (APBO) attributable to:			
Retirees	\$	79,935	\$ 63,749
Fully eligible plan participants		22,812	44,399
Other active plan participants		28,877	34,892
Total APBO		131,624	143,040
Plan assets at fair value		5,545	3,944
APBO in excess of plan assets		126,079	139,096
Unrecognized transition obligation		(109,730)	(117,706)
Unrecognized net prior service cost		(6,003)	(1,458)
Unrecognized net gain (loss)		15,502	(3,811)
Accrued postretirement benefit obligation	\$	25,848	\$ 16,121

The components of the estimated postretirement benefit cost are as follows:

<i>In thousands of dollars</i>	December 31,	1994	1993
Service cost	\$	1,323	\$ 2,746
Interest on accumulated post-retirement benefit obligation		9,666	10,046
Amortization of transition obligation		6,094	6,241
Return on plan assets		(385)	(290)
Amortization of prior service cost		383	—
Amortization of gains and losses		(704)	—
Net postretirement benefit cost		\$16,377	\$18,743

To estimate these costs, health care costs were assumed to increase 11.2 percent in 1995 with the rate of increase declining consistently to 5.75 percent by 2006 and thereafter. The weighted discount rate and salary increase rate were assumed to be 8.5 percent and 5.5 percent, respectively. The expected long-term rate of return on plan assets was 9.0 percent. If the health care cost trend rates were increased by one percentage point, the accumulated postretirement benefit health care obligation as of December 31, 1994 would increase by \$14.7 million while the sum of the service and interest cost components of the net postretirement benefit health care cost for 1994 would increase by \$1.3 million.

12. Postemployment Benefits

In 1992 the Financial Accounting Standards Board released Statement No. 112 (FAS 112), "Employers' Accounting for Postemployment Benefits" which was required to be implemented by January 1, 1994. FAS 112 requires that the projected future costs of providing postemployment, but pre-retirement, benefits, such as disability, pre-pension leave (salary continuation) and severance pay, be recognized as an expense as employees render service rather than when the benefits are paid.

The Company adopted the provisions of FAS 112 effective January 1, 1994. The Company recognized the obligation for postemployment benefits through a cumulative effect charge to net income of \$7.2 million, net of taxes of \$3.9 million. The adoption of FAS 112 is not expected to significantly impact future operating expense or the Company's cash flow.

13. Stock Offering

In February 1994, the Company sold 5.4 million shares of its common stock at \$42 per share in a public offering. As part of the offering, 2.5 million new primary shares were issued and sold directly by the Company and 2.9 million shares were sold by C FON Corporation, a subsidiary of Sprint Corporation. All share and per share data is prior to the 2-for-1 stock split in April 1994.

Values

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10. Postretirement Life and Health Benefits

In addition to providing pension benefits, the company provides health care and life insurance benefits for retired employees. Substantially all of the company's employees may become eligible for those benefits if they reach normal retirement age while working for the company. For the Rochester company, the life insurance benefit for employees who were retired or pension-eligible on September 1, 1981 is provided through a Retired Life Reserve that became fully funded in 1982. With this exception, the health care and life insurance benefits for both the 4,701 active employees and the 1,714 retired employees at December 31, 1992 are provided through insurance companies whose premiums are based on the benefits paid during the year. Through December 31, 1992, the company recognizes the cost of providing those benefits by expensing the portion of the insurance premiums it paid during the year, which was \$14.0 million for 1992, \$12.0 million for 1991 and \$10.8 million for 1990.

In December 1990, the Financial Accounting Standards Board issued Statement No. 106 (FAS 106), "Employers' Accounting for Postretirement Benefits Other Than Pensions," which was implemented by the company on January 1, 1993. FAS 106 requires that projected future costs of providing postretirement benefits, such as health care and life insurance, be recognized as an expense as employees render service instead of when the benefits are paid. Through December 31, 1992, the company recognized the cost of providing postretirement benefits on a pay-as-you-go basis, expensing the costs of postretirement medical insurance premiums and other postretirement benefits in the year paid. The company's accumulated postretirement benefit obligation is \$126.9 million at January 1, 1993. If the delayed recognition of the transition obligation method of adoption is selected, the company estimates that its annual postretirement benefit expense, computed in accordance with FAS 106, will be approximately \$18.3 million versus pay-as-you-go expense of \$4.1 million. If the immediate recognition method is adopted, the annual expense will be approximately \$12.3 million. The accounting method adopted will be influenced by the rate-making treatment as prescribed for the company's regulated telephone operations by federal and state regulatory agencies. The new rules will not negatively impact the company's net cash flow (or its funding strategy) relating to retiree benefits.

11. Postemployment Benefits

In 1992 the Financial Accounting Standards Board released Statement No. 112, "Employers' Accounting for Postemployment Benefits" (FAS 112), which is required to be implemented by January 1, 1994. FAS 112 requires that projected future costs of providing postemployment benefits prior to retirement, such as disability and severance pay, be recognized as an expense as employees render service rather than when the benefits are paid.

The company has not yet decided when it will adopt the new standard or determined the effect that its adoption will have on its financial position and results of operations.

12. Leases and License Agreements

The company leases buildings, land, office space, fiber optic network, computer hardware and other equipment, and has license agreements for rights-of-way for construction and operation of a fiber optic communications system. Total rental expense amounted to \$16.4 million in 1992.

Minimum annual rental commitments under non-cancellable leases and license agreements in effect on December 31, 1992 were as follows:

<i>In thousands of dollars</i> Years	Non-Cancellable Leases		License Agreements
	Buildings	Equipment	
1993	\$ 8,350	\$ 6,930	\$ 6,541
1994	7,661	6,020	6,370
1995	6,926	5,239	6,364
1996	6,495	3,546	6,550
1997	6,764	907	6,512
1998 and thereafter	30,955	—	44,324
Total	\$67,151	\$22,642	\$76,661

13. Business Segment Information

Revenues and sales, operating income, depreciation, construction expenditures and identifiable assets by business segment are set forth in the Business Segment Information included on page 30 of this report.

14. Commitments and Contingencies

In 1984 the New York State Public Service Commission (NYSPSC) initiated a proceeding to investigate the appropriateness of royalty payments from the subsidiaries to Rochester Telephone Corporation for the alleged benefit affiliates gain from using the Rochester Tel name. Prefiled testimony, hearings and briefs were submitted and concluded in the royalty proceeding during 1985. On August 13, 1985, the Administrative Law Judge, in his Recommended Decision, concurred with the royalty concept and indicated that further investigation was necessary to quantify the payment amounts. The royalty proceedings were reopened on May 2, 1990. The company filed a motion for a rehearing of the NYSPSC's May 2, 1990 order reopening the hearings, but the NYSPSC declined to reverse its determination that it possessed the authority to impose a royalty. Nevertheless, the NYSPSC stated that its May 2 order was not final for purposes of judicial review, and it provided additional guidance to the Administrative Law Judge on the scope of hearings on remand. In testimony filed on December 7, 1990, the NYSPSC Staff requested the NYSPSC impose a royalty in the amount of approximately \$11 million per year. The State Consumer Protection Board advocated a royalty of approximately \$14 million per year. These amounts would be treated as an offset to the Rochester company's regulated revenue requirement for ratemaking purposes. On January 15, 1991, the company filed its direct testimony in which it disputed both the justifications for and quantification of the royalty proposals. The Administrative Law Judge released a Recommended Decision on February 3, 1992. Although the Judge concluded that a royalty could be justified as a result of the use of the Rochester Tel name and reputation by Rochester's unregulated subsidiaries, she concluded that the royalty proponents failed to quantify the amount of the royalty. The Judge has recommended that no specific royalty be imposed at this time. In addition, the Judge concluded that the Commission should condition future investments in activities other than Rochester Telephone operations on the payment to ratepayers of a small percentage of the amount of such investments. The Judge also concluded

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10. Service Pensions and Benefits

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The funded status of the plans' is as follows:

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Amount expensed due to regulatory agency actions	(1,537)	6,787	2,223
Net periodic pension cost recognized	\$ (2,708)	\$ 3,050	\$ 3,336

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is computed for financial reporting purposes and may differ from the actuarial determination for funding due to varying assumptions and methods of computation.

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In adopting FAS 106, the company elected to defer the recognition of the accrued obligation of \$125 million over a period of twenty years. For 1993, the adoption of this standard resulted in additional operating expenses in the amount of \$7.8 million, net of a deferred income tax benefit of \$4.1 million. However, a substantial portion of this increase was offset by a change in accounting for pensions for rate making purposes at the Rochester company. The change requires that the company amortize, over a ten year period, the cumulative amount of pension funding from January 1, 1987 over the amount of pension expense which would have been recognized through December 31, 1992 under FAS 87, reducing pension expense throughout the amortization period. The net impact of adopting FAS 106 and recording the accounting change for FAS 87 actually resulted in only \$3.8 million of additional operating expenses, net of the income tax benefit, in 1993.

Proxy Statement

1994 Financial Review

frontier

**Notice of Annual Meeting of Shareowners
To be Held on April 26, 1995**

Dear Shareowners:

The first Annual Meeting of Shareowners of Frontier Corporation (the "Company") will be held at the National Press Club, 14th and F Streets, N.W., Washington, D.C. 20045, at 10:00 a.m. on April 26, 1995, for the following purposes:

- To elect nine Directors;
- To consider and act upon a proposal to elect Price Waterhouse LLP as the Company's independent auditors for the fiscal year ending December 31, 1995;
- To consider and act upon two proposals regarding employee and director compensation plans; and
- To transact such other business, if any, as may properly come before the meeting or any adjournments thereof.

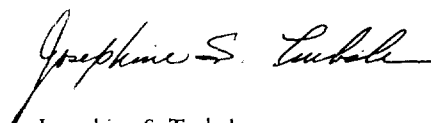
The Board of Directors, on December 19, 1994, amended Article II, Section 2, of the By-Laws to reduce the number of Directors constituting the entire Board from twelve to nine, effective January 1, 1995.

The Board of Directors has fixed the close of business on March 7, 1995, as the record date for the determination of shareowners entitled to notice of and to vote at the meeting.

Your vote is very important. Please sign and date the enclosed proxy card and return it promptly in the enclosed return envelope, whether or not you expect to attend the meeting. You may revoke your proxy and vote in person if you decide to attend the meeting.

If you are planning to attend the annual meeting, please check the box on the back of the proxy card.

By Action of the Board of Directors,



Josephine S. Trubek
Corporate Secretary
Rochester, New York
March 13, 1995

of Income. Previously, the revenues and expenses of the Company's wireless operations in New York had been consolidated. (See Note 3 to the Consolidated Financial Statements.)

In May 1994, we sold our only telephone operating company in North Dakota, Minot Telephone, for cash. Minot served approximately 27,000 access lines. The transaction resulted in a pre-tax gain of \$11.3 million.

In December 1993, the Company increased its cellular ownership from 50.6 percent to 69.6 percent in the South Alabama cellular partnership. This transaction gave the Company the right to manage the two cellular properties, Alabama RSA #4 and #6, which serve a territory with a population of approximately 252,000. As a result of this increased ownership, we began reporting the South Alabama cellular interests on a consolidated basis of accounting in 1994, whereas previously this partnership had been accounted for on the equity method.

In September 1993, Frontier Communications of the Mid Atlantic, Inc. (formerly Mid Atlantic Telecom, Inc.) was acquired using 143,587 shares of treasury stock (before the 1994 stock split). In June 1993, we acquired Budget Call Long Distance, Inc. for \$7.5 million in cash. Both transactions were accounted for as purchase acquisitions.

Also in September 1993, the Company sold its interest in the S&A Telephone Company in Kansas (approximately 800 access lines) and its related minority cellular interest. In addition, the Company sold a substantial portion of its investment in a Canadian long distance company in November 1993. These sales resulted in pre-tax gains totaling \$4.4 million.

In April 1993, we acquired a 70 percent ownership interest in the Utica-Rome Cellular Partnership by issuing 702,737 shares of the Company's common stock (before the 1994 stock split). We recorded this transaction using the purchase method of accounting.

In August 1992, we acquired Frontier Communications of Georgia (formerly Statesboro Telephone Company), a company with more than 15,000 access lines. A total of 1.5 million shares of common stock were issued in the transaction (before the 1994 stock split), which was accounted for as a pooling of interests.

2. Accounting for Postemployment Benefits

The Company changed its method of accounting for certain employee benefits in 1994. This change was necessitated by the Financial Accounting Standards Board, the authoritative body for accounting rules. This new rule, referred to as Financial Accounting Standards Board Statement No. 112 (FAS 112), "Employers' Accounting for Postemployment Benefits," addresses the manner in which companies must record expenses for postemployment benefits, including payments for disability, pre-pension leave (salary continuation) and severance pay. FAS 112 requires

that projected future costs of providing postemployment benefits be recognized as an expense as employees render service rather than when the benefits are paid. This accounting change is very similar to the change made in 1993 for postretirement benefits, which was addressed by FAS 106, "Employers' Accounting for Postretirement Benefits Other than Pensions." Adoption of FAS 112 required the Company to calculate, and record in 1994, the cumulative effect of the change in accounting methodology for all years prior to 1994. The cumulative effect of the change in accounting methodology for FAS 112 amounted to an after-tax charge of \$7.2 million, net of taxes of \$3.9 million. As required by the pronouncement, the Company reported this one-time charge as a special line item on the Consolidated Statement of Income in 1994. This accounting change does not have a material impact on the Company's cash flows or its earnings from continuing operations.

3. Tax Rate Change

The 1993 income tax provision includes the retroactive impact of the federal income tax rate increase from 34 percent to 35 percent. The overall impact of the tax rate change was approximately \$2 million and includes approximately \$400,000 attributable to years prior to 1993. (See Note 9 to the Consolidated Financial Statements.)

4. Software Write-Off

In 1993, the Company recorded a \$3.3 million pre-tax charge to write-off certain deferred costs associated with a project to redesign customer account records, order flow and customer billing systems. (See Note 5 to the Consolidated Financial Statements.)

5. First Mortgage Bond Refinancing

In 1992, the Company recorded an extraordinary, after-tax charge of \$1.1 million relating to costs incurred for the early extinguishment of its Series H, 9½% first mortgage bonds. The bonds were retired using internally generated cash and the private placement of \$35 million of debt at a telephone subsidiary. (See Note 5 to the Consolidated Financial Statements.)

Telecommunication Services

The Telecommunication Services segment is comprised of the Company's long distance business, wireless operations (where the Company has sufficient ownership to report on a consolidated basis), and equipment sales. This segment is the fastest growing part of the Company, as evidenced by its increasing contribution to our overall financial results. In 1994, revenues from Telecommunication Services comprised 38 percent of total revenue, up from 29 percent only two years ago. Similarly, operating income from this business segment accounted for 18 percent of the Company's total, as compared with 13 percent in 1992.